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No. 10090

United States

14/42 Circuit Court of Appeals

For the Ninth Circuit.

SAMUEL POORMAN, JR.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of the Record

Upon Petition to Review a Decision of the United States
Board of Tax Appeals.

FILED

MAY 11 1942

PAUL P. O'BRIEN,

CLERK

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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APPEARANCES

For Taxpayer:

Pro se

For Comm'r:

B. M. COON, Esq.

Docket No. 102994

SAMUEL POORMAN, JR.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1940

May 27—Petition received and filed. Taxpayer notified. Fee paid.

“ 27—Copy of petition served on General Counsel.

“ 27—Request for Circuit hearing in Los Angeles filed by taxpayer. 5/27/40 copy served.

Jul. 22—Answer filed by General Counsel.

“ 25—Copy of answer served on taxpayer. Los Angeles, Calif.

Dec. 30—Hearing set Feb. 17, 1941 in Los Angeles, Calif.

1941

Feb. 18—Hearing had before Mr. Mellott on the merits. Submitted. Petitioner's brief due April 4, 1941—respondent's May 19, 1941 and petitioner's reply June 3, 1941.

Mar. 5—Transcript of hearing of Feb. 18, 1941 filed.

Apr. 1—Brief filed by taxpayer. 4/1/41 copy served.

“ 25—Reply brief filed by General Counsel.

May 20—Reply brief filed by taxpayer. 5/20/41 copy served.

Sep. 12—Findings of fact and opinion rendered, Mr. Mellott. Decision will be entered for the respondent. 9/16/41 copies served.

“ 16—Decision entered, Mellott, Div. 11.

Dec. 5—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by taxpayer.

“ 5—Affidavit of service by mail filed by taxpayer.

“ 12—Statement of evidence filed by taxpayer.

“ 27—Motion for extension to Feb. 16, 1941 to prepare and transmit record filed by taxpayer. 12/30/41 motion returned to taxpayer.

1942

Jan. 10—Praecipe for record filed by taxpayer.

“ 12—Order from 9th Circuit granting motion for extension to Feb. 16, 1942 to prepare and transmit record filed.

1942

Jan. 13—Proof of service of praecipe filed.

Feb. 12—Order from 9th Circuit granting motion
for extension to March 16, 1942 to pre-
pare and transmit record filed.

Mar. 3—Agreed statement of evidence filed. [1*]

United States Board of Tax Appeals

Docket No. 102994

SAMUEL POORMAN, JR.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency IT:LA PAK-90D, dated March 27, 1940, and as a basis for his proceeding, alleges as follows:

I.

The petitioner is an individual with residence at Hotel Mayfair, No. 1256 West Seventh Street, in the City of Los Angeles, State of California, and

*Page numbering appearing at foot of page of original certified Transcript of Record.

office at No. 207 South Broadway in said City. The return for the period here involved was filed with the Collector for the Los Angeles Division, Sixth District of California. [2]

II.

The Notice of Deficiency, (a copy of which is attached and marked "Exhibit A"), was mailed to the petitioner on March 27, 1940.

III.

The taxes in controversy are income taxes for the calendar year 1937, and in the amount of \$708.92.

IV.

The determination of tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The inclusion in taxable income, (as additional income), of the sum of \$8,394.92 paid to the petitioner by Los Angeles Gas and Electric Corporation.

(b) The disallowance as a deduction from gross income of the sum of \$18.45, constituting a loss by casualty sustained by the petitioner.

(a) The inclusion of \$8,394.92 in taxable income.

(1) From June 1, 1920, to January 31, 1937, inclusive, the petitioner was employed as an attorney at law in the Legal Department of Los Angeles Gas and Electric Corporation, a corporation duly organized and existing under and by virtue of the laws of the State of California. [3]

(2) During such period said Los Angeles Gas and Electric Corporation owned and operated a public utility gas system and also a public utility electric system, which systems respectively served, inter alia, said The City of Los Angeles and its inhabitants with gas and electricity.

(3) Pursuant to an agreement of purchase and sale theretofore made between said Los Angeles Gas and Electric Corporation, as vendor, and The City of Los Angeles, as vendee, said electric system of said Corporation was sold and transferred by said Corporation to The City of Los Angeles at twelve o'clock midnight on January 31, 1937. That said electric system ever since has been, and now is, owned by said The City of Los Angeles, and has been, and now is, under the control and management of the Department of Water and Power, a department of said The City of Los Angeles that, under the Charter of said City, has the power and duty of such control and management.

(4) Coincidentally with the sale and transfer of said electric system by said Los Angeles Gas and Electric Corporation to said The City of Los Angeles, as aforesaid, to wit, on January 31, 1937, the petitioner's said employment by said Los Angeles Gas [4] and Electric Corporation wholly ceased and terminated, and the petitioner was, on January 30, 1937, paid in full for all services by him rendered and to be rendered during the month of January, 1937, pursuant to his contract of em-

ployment with said Los Angeles Gas and Electric Corporation, and had theretofore been paid in full for all services by him rendered or to be rendered by said Los Angeles Gas and Electric Corporation pursuant to his said contract of employment for the period of such employment prior to January 1, 1937.

(5) On or about February 19, 1937, Los Angeles Gas and Electric Corporation paid the petitioner said sum of \$8,394.92, but such payment was made without any consideration whatsoever, either for past services rendered by the petitioner, or for future services to be rendered by petitioner, or otherwise; and the said sum accordingly constituted a mere gift and as such was and is non-taxable income.

(6) In determining said supposed deficiency, the respondent ruled that such gift constituted taxable income for the calendar year 1937, upon the ground that the payment thereof had been claimed by said Los Angeles Gas and Electric Corporation as an operating expense, to wit, additional compensation for past [5] services rendered to said Corporation by the petitioner.

(7) The ruling of the respondent last aforesaid was and is erroneous and contrary to the decision of the Supreme Court of the United States in the case of *Bogardus v. Commissioner of Internal Revenue*, 302 U. S. 34; 82 L. Ed. 32 (decided November 8, 1937).

(b) The disallowance of \$18.45 as a deduction from gross income.

(1) During the year 1937, shortly prior to November 15th, the petitioner accidentally broke a pair of eyeglasses with their frame, upon the use of which the petitioner was and is continuously dependent.

(2) Thereafter on November 15, 1937, said eyeglasses were replaced by the petitioner at a cost to him then paid of \$18.45.

(3) The petitioner has been unable to ascertain either the date of the acquisition by him of the glasses so broken or the cost of the same, but that according to his best recollection the date of such acquisition was within a year or two prior to said November 15, 1937, and said cost was slightly in excess of said sum of \$18.45.

(4) In determining said supposed deficiency, the respondent disallowed the said sum of \$18.45 claimed [6] by the petitioner as a deduction from gross income in the year 1937, upon the grounds (a) that the same did not and does not constitute a deduction within the meaning of Section 23(e) of the Revenue Act of 1936; and (b) that such claim deduction had not and has not been substantiated, nor has the amount of the alleged loss been established.

Wherefore, the petitioner prays that this Board may hear the proceeding and, by its determination therein,—

(a) Exclude from taxable income of the petitioner, for the calendar year 1937, the said sum of

\$8,394.92 as constituting a gift in said year, received by the petitioner from said Los Angeles Gas and Electric Corporation, as aforesaid;

(b) Allow as a deduction from gross income of the petitioner, for the calendar year 1937, the said sum of \$18.45 as constituting a loss by casualty sustained by the petitioner.

SAMUEL POORMAN, JR.

Petitioner, in propria persona,
P. O. Box 240, Arcade Annex,
Los Angeles, California. [7]

State of California,
County of Los Angeles—ss.

Samuel Poorman, Jr., being duly sworn, says that he is the petitioner above named; that he has read the foregoing petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

SAMUEL POORMAN, JR.

Subscribed and sworn to before me, this 21 day of May, 1940.

(Seal) EVERARD L. McMURRIN
Notary Public in and for the County of Los Angeles,
State of California. [8]

“EXHIBIT A”

Treasury Department
Internal Revenue Service
12th Floor,
U. S. Post Office and Court House,
Los Angeles, California.

Mar. 27, 1940

Office of
Internal Revenue Agent in Charge
Los Angeles Division

IT:LA
PAK-90D

Mr. Samuel Poorman, Jr.,
207 South Broadway,
Los Angeles, California.

Sir:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1937 discloses a deficiency of \$708.92 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are

requested to execute the enclosed form and forward it to Internal Revenue agent in Charge, Los Angeles, California, for the attention of IT:LA:FC. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlied.

Respectfully,

GUY T. HELVERING,

Commissioner,

By R. B. SULLIVAN,

Internal Revenue Agent

Enclosures:

Statement.

Form of waiver. [9]

STATEMENT

Mr. Samuel Poorman, Jr.

207 South Broadway,

Los Angeles, California.

Tax Liability for the Taxable Year Ended

December 31, 1937

Income tax—

Liability—\$816.97

Assessed—\$108.05

Deficiency—\$708.92

In making this determination of your income tax liability, careful consideration has been given to

the report of examination dated September 11, 1939; to your protest dated September 19, 1939; and to the statements made at the conferences held on November 9, 1939 and February 5, 1940.

Adjustments to Net Income

Net income as disclosed by return.....		\$ 4,801.23
Additional income and unallowable deductions:		
(a) Additional compensation	\$8,394.92	
(b) Loss by casualty.....	18.45	8,413.37
	<hr/>	<hr/>
Net income adjusted.....		\$13,214.60

Explanation of Adjustments

(a) The amount of \$8,394.92 paid to you by the Los Angeles Gas and Electric Corporation in 1937 has been included in your gross income for the calendar year 1937 pursuant to the provisions of section 22(a) of the Revenue Act of 1936.

(b) The amount of \$18.45 which you claimed as a deduction in the year 1937 through the accidental breakage of your eyeglasses has been disallowed as not constituting a deduction within the meaning of section 23(e) of the Revenue Act of 1936, and for the further reasons that such claimed deduction has not been substantiated nor has the amount of the alleged loss been established.

The earned income credit has been increased to \$965.94 in accordance with section 25(a)(3) of the Revenue Act of 1936. [10]

Computation of Tax

Net income adjusted.....		\$13,214.60
Less: Personal exemption	\$1,000.00	
Credit for dependents.....	800.00	1,800.00
		<hr/>
Balance (surtax net income).....		\$11,414.60
Less: Earned income credit.....		965.94
		<hr/>
Net income subject to normal tax.....		\$10,448.66
Normal tax at 4% on \$10,448.66.....	\$417.95	
Surtax on \$11,414.60.....	399.02	
		<hr/>
Correct income tax liability.....		\$816.97
Income tax assessed:		
Original, account #820708.....		108.05
		<hr/>
Deficiency of income tax.....		\$708.92

[Endorsed]: U. S. B. T. A. Filed May 27, 1940.

[11]

[Title of Board and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

I, II, III.

Admits the allegations contained in paragraphs I, II and III of the petition.

IV(a)(b)

Denies the Commissioner erred as alleged in subdivisions (a) and (b) of paragraph IV of the petition.

Reference is made to subdivisions (a) (1) to (7), inclusive, of Paragraph IV of the petition. Respondent admits that during part of the year 1937 the petitioner was employed as an attorney in the legal department of the Los Angeles Gas and Electric Corporation which owned and operated a public utility gas and *and* electric system in Los Angeles, California; and further admits that on or about January 1, 1937, the petitioner received from said [12] corporation a certain sum, the amount of which is not known to this respondent, as fees, salary and compensation for services rendered prior to that date, but denies that such payment, or payments, was in full satisfaction for all services theretofore rendered by the petitioner to the said gas and electric corporation.

Respondent denies each and every other allegation contained in subdivisions (a) (1) to (7), inclusive, of said petition, and specifically denies that the amount of \$8,394.92 received by the petitioner in February, 1937, and any other amounts received by the petitioner from said Los Angeles Gas and Electric Corporation on and after the first day of January, 1937, was a gift to petitioner from said corporation.

Reference is made to subdivisions (b) (1) to (4), inclusive, of paragraph IV of the petition. Re-

spondent admits that on or about February 19, 1937, the said petitioner received from the Los Angeles Gas and Electric Corporation a sum not less than \$8,394.92 as additional fees, salary and compensation for services theretofore rendered the said gas and electric corporation. Respondent denies each and every allegation therein contained, except the statements that petitioner claimed as a deductible loss from his 1937 income the amount of \$18.45 on account of the loss of eyeglasses through casualty and that the respondent disallowed said claim.

V.

Denies each and every allegation contained in the petition not hereinbefore specifically admitted or denied. [13]

Wherefore, it is prayed that the determination of the Commissioner be approved.

J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

FRANK T. HORNER,

B. M. COON,

Special Attorneys,

Bureau of Internal Revenue.

BMC/c 7-16-40

[Endorsed]: U. S. B. T. A. Filed Jul. 22, 1940.

[14]

[Title of Board and Cause.]

Under the evidence it is *held* that the payment of a substantial sum to the petitioner by his former employer constituted additional income rather than a gift. *Bogardus v. Commissioner*, 302 U. S. 34, distinguished.

Samuel Poorman, Jr., Esq., pro se.

Byron M. Coon, Esq., for the respondent.

This proceeding involves a deficiency in income tax for the calendar year 1937 in the amount of \$708.92. The issue is, Did the respondent err in including in petitioner's gross income \$8,394.92 received by him from his former employer under the circumstances hereinafter set out?

FINDINGS OF FACT.

Petitioner is a resident of Los Angeles, California. He filed his income tax return for the year 1937 on the basis of cash receipts and disbursements with the collector of internal revenue for the sixth district of California.

Petitioner is an attorney at law, employed by the city of Los Angeles and assigned to duty with the department of water and power. For a period of approximately 17 years preceding January 31, 1937, petitioner had been employed in the legal department of the Los Angeles Gas & Electric Corporation. For approximately 10 years prior to the termination of petitioner's employment by this corpora-

tion he had been exclusively engaged in defending and working upon litigation which had been instituted by the city of Los Angeles and by the city of Pasadena against it. The general purpose of the litigation was to enjoin the corporation from using the cities' streets for the distribution of gas and electricity or for any purpose other than lighting.

During 1935 negotiations were begun looking to the sale of the electric properties of the corporation. This culminated in the execution of a final agreement in October 1936, under which such properties were sold [15] to the city as of January 31, 1937, for approximately \$46,000,000. In connection with the sale approximately 840 employees of the corporation, chiefly those who had been engaged in the operation of the electric properties, were transferred to the department of water and power of the city of Los Angeles. Petitioner was one of those transferred, although he did not enter the employ of the city department until March 1, 1937. The transferred employees constituted about one-third of the personnel of the corporation. After the sale of the electric properties the corporation engaged solely in the gas business. In May 1937 it was merged with the Southern California Gas Co.

On May 30, 1937, petitioner, whose salary from 1929 forward had been \$1,000 a month, was paid in full by the Los Angeles Gas & Electric Corporation for all services rendered and to be rendered by him during the month of January 1937. He had there-

tofore been paid in full by the corporation for all services rendered by him prior to January 1, 1937. Attached to the check by which such payment for services for January 1937 was made, was a voucher containing the following statement:

Statement of Account. In full settlement of which payee has accepted Los Angeles Gas & Electric Corporation check, annexed hereto: Samuel Poorman, Jr., January 30, 1937, services as attorney during the month of January, 1937,—\$1,000.00. Payee will detach and retain this statement.

In September of 1932 the corporation and several other public utility companies in southern California established a "Uniform Pension and Benefit Plan" for their employees. A booklet was printed explaining the details of the plan, which in general provided: That each employee should contribute by pay roll deduction each month 3 percent of his current wages, to be "used solely to provide a portion of his total retirement income." The company was to pay the entire balance of the net cost of the employees' retirement income and in addition provide and administer at its own expense the death and disability benefits. The printed announcement states: "The companies believe in this plan so firmly that their contract with the insurance company provides that the companies' contributions, once made to these funds, must be used for employee benefit only and not diverted to any other purpose. In other

words, the companies' payments, as well as the employees' deposits, are dedicated solely to the cause of employee benefit."

All employees who had completed two or more years of continuous service prior to September 1932 were eligible to participate in the plan. Employees completing 10 or more years of continuous service prior to normal retirement date (65 for men and 60 for women) were entitled to receive a monthly pension of \$1 per month for each \$1,000 of wages earned during continuous service subsequent to September 1, 1930, the [16] minimum pension for those who completed 20 or more years of continuous service at normal retirement date being \$45 per month. Such pension payments were to commence on the last day of the month following retirement and continue during the life of the employee. Each employee's contribution under the plan was to be paid over to the insurance company and used to provide a portion of his retirement income. The amount was returnable to the employee in cash if he should leave the employ of the company or to his beneficiaries in cash if he should die prior to reaching retirement age.

The company obligated itself to pay the entire balance of the net cost of the employee's retirement income and in addition to provide and administer at its own expense the death and disability benefits. The death benefit was to be an amount equal to one year's wages, with a minimum of \$2,000

for full-time employees. The disability benefits were to be "3 percent per month of the total death benefit in effect at the date the disabled employee leaves work on account of disability", payments at this rate to continue for 12 months. For the next 48 months payments were to be made at the rate of $2\frac{1}{2}$ percent per month of the total death benefit. The maximum monthly disability benefit was not to exceed 50 percent of the monthly salary in effect at the date the employee should leave work on account of disability. The disability payments were to be "inclusive of any disability payments made pursuant to the Workmen's Compensation, Insurance and Safety laws of the State of California, and/or any laws of said State providing disability compensation." For employees who would have completed 20 or more years of continuous service at normal retirement date, the minimum disability benefit or disability retirement income was to be \$45 per month, and employee contributions were to cease during the period of disability. If an employee withdrew or was released from service prior to normal retirement age, he had the option of converting his death benefit into any of the regular life insurance policies issued by the insurance company, except term insurance, at the rate applicable to his then attained age and class of risk. Such conversion could be effected without medical examination, provided application be made within 31 days after termination of service. The company reserved the right to discontinue or change the plan at any

time. "Discontinuance or change, however, will neither deprive any employee of any right with respect to his contributions nor affect retirement annuities which have been purchased prior to the date of discontinuance or change. The Companies' contributions, once made, will be used for employees' benefits and for no other purpose."

When it became obvious that the sale would be consummated and a substantial number of the corporation's employees would be transferred, serious consideration was given by the corporation's officers [17] to the effect of the transfer upon the rights of the employees under the "Uniform Pension and Benefit Plan." It was recognized that the employees were losing various rights in leaving the service of the corporation and that "severance of employment meant sacrifice of pension rights." The officers wanted to do something for the employees who were to be transferred "in consideration of the fact that they were going to lose their pension rights by termination of service." They first considered the possibility of obtaining from the insurance company which had underwritten the plan some sort of continuing benefit under it. The representatives of the insurance company told them this would be impossible, and that they "had just better forget any such thing as that, and do directly for the departing employees whatever the company could and desired to do." After much discussion and study, the corporation decided in the latter part of November or early in December 1936 to make a payment

to each of the transferred employees based upon his or her age, length of service with the company, and wages received during period of employment. The "tax angle" was taken into consideration also, and it was decided to make the payment in such a manner that it would be a proper deductible expense of the corporation in computing the net profit from the sale. Careful consideration was given to the language describing the payments in the checks to be issued and in letters to be sent to the transferred employees. It was decided that the words "additional compensation" would accurately describe the payments "inasmuch as the extra compensation was based on the length of past service, that is, service prior to January 31, 1937, [and] upon the rate of the pay received by the employee during all that period."

On or about January 25, 1937, the Los Angeles Gas & Electric Corporation sent two letters to each of the employees to be transferred. One, dated January 25, 1937, signed by its president and general manager, was addressed: "To Employees about to be transferred from the service of our Company:". It contained the following statement:

Arrangements have been made to grant you additional compensation in recognition of the value of your past services. The amount of this payment will be based upon your present attained age, your length of service with the Company, and the rates of wages received during

your period of employment; but this extra compensation will not be paid to employees whose "employment date" is more recent than September 1, 1934. Checks will be mailed to you as soon as possible after our electric properties have passed to the City.

The other letter dated, January 1937, was addressed "To Members of Uniform Pension and Benefit Plan Who Will Transfer to the Service of the City of Los Angeles concurrently with the Transfer of Our Electric System to the City:" and informed them that their membership in the uniform pension and benefit plan would cease with [18] the termination of their service; that their life insurance protection under the plan would continue for 31 days after termination of service; and that a check would be sent covering the amount of their contributions to the plan, together with interest thereon.

Petitioner received these two letters sometime after January 25, 1937. On that date he was notified by the president of the Los Angeles Gas & Electric Corporation that his work with the corporation was finished and that he was to be transferred to the department of water and power of the city of Los Angeles. In the course of this conversation, the president of the corporation stated that the Pacific Lighting Corporation had arranged for the giving of a bonus to the employees who were to be transferred to the city department. The Pacific Lighting Corporation was the holding company of which the

Los Angeles Gas & Electric Corporation was the principal subsidiary. The holding company owned all of the common stock of such subsidiary, and completely dominated the management and control of it. At all times during the petitioner's employment by the subsidiary its earnings sufficed to cover several times its preferred stock dividends.

On or about February 19, 1937, the petitioner received from the Los Angeles Gas & Electric Corporation a check for \$8,394.92, to which was attached a voucher reading as follows:

Additional compensation for services to and including January 31, 1937, in accordance with the President's letter of January 25, 1937. No. 26, Total amount, \$8,491.34. Deductions, Federal O. A. B., \$20. State, U. I., \$76.42. Net amount, \$8,394.92 This statement constitutes a valuable record of your earnings and the contributions you have made toward future social security benefits We recommend that you keep it for your *further* reference. Los Angeles Gas & Electric Corporation, detachable for presenting for payment.

The payments made by the Los Angeles Gas & Electric Corporation to the employees transferred to the department of water and power of the city of Los Angeles, in accordance with the letter of January 25, 1937, aggregated \$475,546.32, and were charged to a ledger account designated "Sale of Electric Properties, Suspense Account." This ac-

count showed in black entries the total expenses in connection with the sale of the properties, and in red ink figures the amount received from the city for them, together with any other credits necessary in order to arrive at the net profit. On the books of the corporation the payments of \$475,546.32 were treated as an expense incurred in connection with the sale of the electric properties. In the corporation's income tax return for 1937 these payments were treated in the same manner and were deducted from the amount received from the city in computing the net profit realized from the sale of the electric properties.

No bonus or additional compensation whatsoever was paid to the employees retained by the Los Angeles Gas & Electric Corporation, [19] and no extra payment other than the one here in question was ever made by the corporation to the petitioner.

The petitioner had nothing to do with the sale of the electric properties, nor did any other employee of the corporation who was transferred to the department of water and power and to whom the so-called additional compensation was paid.

In petitioner's individual income tax return for the calendar year 1937, the amount of \$8,394.92 was reported in a schedule as nontaxable income other than interest. The following explanation was given: "Bonus received from Los Angeles Gas & Electric Corporation after leaving its employ upon transfer of its electric system to The City of Los Angeles,

(not having been paid or received as a consideration for services rendered, and the same constituting a gift, as held in *Bogardus v. Commissioner of Internal Revenue* [302 U. S. 34], 82 L. Ed. 90); * * * \$8,394.92.”

Respondent determined that the \$8,394.92 was additional compensation and added this amount to the net income shown in petitioner's income tax return for 1937.

OPINION.

Mellott: Petitioner, in support of his contention that the \$8,394.92 was a gift, relies principally upon *Bogardus v. Commissioner*, 302 U. S. 34. In that case, the taxpayer, prior to 1931, had been in the employ of the Universal Oil Products Co., the business and assets of which had greatly increased between 1922 and 1930. Early in 1931, its entire stock was sold to the United Gasoline Corporation for \$25,000,000. Prior to the sale, and in contemplation of it, the Unopco Corporation had been organized for the purpose of acquiring, and it did acquire, certain assets of the Universal Co. of the value of over \$4,000,000. All of the former stockholders of the latter company became stockholders of Unopco, with the same proportionate holdings. None of them, after the sale of the Universal stock, held any stock in the Universal Co. or in the United Gasoline Corporation. Under its new ownership, the Universal Co. continued to carry on the same business, retaining a large part of its assets. A few days after the

sale of the Universal Co.'s stock, the former stockholders, then stockholders of the Unopco Co., held a meeting at which it was proposed that they show their appreciation of the loyalty and support of some of the employees of the Universal Co. by making them a "gift or honorarium." At meetings of the board of directors and stockholders of Unopco resolutions were adopted that \$607,500 be appropriated, paid, and distributed as a bonus to 64 former and present employees of the Universal Co., in recognition of their valuable and loyal services. Bogardus continued to remain in the employ of the Uni- [20] versal Co. after the change of the ownership of its stock, and when the distribution was made by Unopco in 1931 he received \$10,000. The Supreme Court held that this payment was a gift and not additional compensation.

There are several differences between the facts in the Bogardus case and those presently before us. "The recipients of the bounty * * * were never employees of the Unopco Company, or any of its stockholders." Petitioner and the other employees who received the payments from the corporation had been in its employ until the sale of the properties to the city. "Neither the Universal Company nor any one else was under any obligation, legal or otherwise, to pay any of the recipients, including petitioner, any salary, compensation, or consideration of any kind." The Los Angeles Gas & Electric Corporation, however, was at least under a moral obliga-

tion to the employees whose services were being terminated through no fault of theirs. It had agreed with them "to provide and administer, at its own expense, the death and disability benefits" and to pay a portion of the net cost of securing a "retirement income." Though the record does not disclose the exact amount which the company had contributed and which "once made, * * * [was to] be used for employees' benefits and for no other purpose", it must have been a considerable amount. Petitioner's rights, for example, seem to have been to receive "retirement income" of at least \$76 per month, insurance of at least \$12,000, and disability benefits of \$360 per month for 12 months and \$300 per month for an additional 48 months. "It was recognized", said the vice president of the company and chairman of the benefit committee, "that in accordance with the terms of the pension plan, severance of employment meant sacrifice of pension rights except, I would say not only pension rights, but all rights under the pension benefit plan, with the exception that the life insurance in accordance with the regular provisions always continued for 31 days after termination of service. It was recognized that the employees were losing various rights in leaving the service of the corporation." For this reason "consideration commenced among the company officials as to what, if anything, could be done for the employees who were transferred to the city with the property * * * in consideration of the fact that they

were going to lose their pension rights by termination of service." "Finally, after much discussion and study of the situation, the plan which was ultimately followed was worked out and a basis of compensation, additional compensation for past services, was formulated which, as stated in the President's letter, was in consideration of past valuable services and was based upon the present attained age of the employees, their length of service [21] with the company, and the rates of wages which they had received during their period of employment."

In the Bogardus case the payments were charged "not to expense but to surplus." In the instant proceeding the payments were charged to expenses in connection with the sale of the properties. Here again the record is not very clear; but inferentially it seems that the charge could properly have been so classified only if it had been necessary for the corporation to make the payments either to fulfill an obligation (even "a moral obligation, however slight", *Bogardus v. Commissioner*, *supra*), or to regain possession of some of the money which had been put up with the understanding it would "be used for employees' benefits and for no other purpose." It is also not without significance that the payments in the instant proceeding were designated by the corporation "additional compensation" while those in the Bogardus case were referred to as part of a "gift or honorarium" to the employees. True, calling a payment a gift, bonus, honorarium, additional compensation, or anything else does not

change, or establish, its true characteristic; but it is at least a circumstance to be considered in determining the intention of the parties. "Intention" said the Court in the *Bogardus* case, "must govern." The Court was referring to the intention of the one making the payment. The Circuit Court of Appeals for the Ninth Circuit indicated in *Botchford v. Commissioner*, 81 Fed. (2d) 914, that it felt that the intention of the employer was particularly important—a view evidently shared by other Circuit Courts, *Fisher v. Commissioner*, 59 Fed. (2d) 192; *Walker v. Commissioner*, 88 Fed. (2d) 61; *Levey v. Helvering*, 68 Fed. (2d) 401; *Bass v. Hawley*, 62 Fed. (2d) 721, and also by this Board. Cf. e. g. *N. H. Van Sicklen, Jr.*, 33 B. T. A. 544. Then, too, as the court pointed out in *Botchford v. Commissioner*, *supra*, as a general rule directors of a corporation have no power or authority to give away any of its assets, cf. *Noel v. Parrott*, 15 Fed. (2d) 669; certiorari denied, 273 U. S. 754; and "if the directors could not give away this sum, and the books of the corporation show that it was not given away, it must be presumed that the payment was not a gift."

Whether the payment to this petitioner was, or was not, a gift is a mixed question of law and fact. Respondent determined that it was not a gift. Petitioner, undertaking to overcome the presumption attaching to this determination, *Botany Worsted Mills v. United States*, 278 U. S. 282, has shown and it has been found as a fact that he, previous to the receipt of the sum in issue, had received all of

his agreed salary. He argues that the additional payment not only was not "additional" compensation, but that it could not even be "compensation", since he had already been compensated in full. [22] In *Botchford v. Commissioner*, *supra*, the court quoted with approval the following language used by the Circuit Court of Appeals for the Second Circuit in *Fisher v. Commissioner*, *supra*:

The doctrine that bonus payments and gratuitous "additional compensation" for past services may constitute taxable income has been frequently recognized in decisions of the lower Federal courts and of the Board of Tax Appeals.

We do not interpret the *Bogardus* case as laying down any different principle. Cf. *Georgia S. Williams*, 36 B. T. A. 974.

Petitioner also contends that, since the corporation saw fit to enter the payment made to him and to the other employees upon its books as an expense item in connection with the sale of its electric properties, and since the evidence shows that they, and especially he, had nothing to do with making such sale, it follows that the corporation erred in characterizing the payment as additional compensation. There would be more substance to this contention if the respondent were required to prove that the payment was made in consideration of, and as compensation for, services rendered by petitioner in that particular transaction. But he had no such burden.

He may rest upon the presumption of correctness attaching to his determination that the payment was not a gift, *Botany Worsted Mills v. United States*, *supra*; *Reinecke v. Spalding*, 280 U. S. 227; and petitioner must prove that this determination was erroneous. He has not sustained his burden merely by proving—if in fact he has proved—that it was improperly treated upon the books of the corporation. In other words, it was incumbent upon petitioner to prove that the corporation was not discharging some obligation to him by making the payment in question. The evidence indicates that the payments were made to compensate the employees for the loss of their rights under the “Uniform Pension and Benefit Plan” or to enable the company to withdraw the funds which had been put up with the insurance company in connection with such plan. This, in our opinion, was sufficient consideration to prevent the payments being absolute gifts. We therefore hold that the respondent committed no error in including the amount received by this petitioner in his gross income.

The only other error charged in the petition is the disallowance by the respondent of a deduction of \$18.45. This is not discussed upon brief. The petition alleges that petitioner accidentally broke a pair of eyeglasses with their frame and replaced them during the taxable year at a cost of \$18.45; that he had been unable to ascertain either the date of the acquisition of the glasses so broken or their cost; and

that according to his best recollection the date of acquisition was within a year or two prior to their replacement, the cost being in excess of \$18.45.

At the hearing petitioner admitted he did not have any "very satisfactory proof" that he had sustained a loss through casualty. (Sec. [23] 23 (e) (3), Revenue Act of 1936.) He testified that he had paid \$3 of the \$18.45 to a doctor for examination of his eyes, \$15 for new glasses, and 45 cents as state tax. This was the sole evidence offered. The claim for the deduction has probably been abandoned; but, if not, this issue must be resolved against petitioner for failure of proof.

Decision will be entered for the respondent. [24]

United States Board of Tax Appeals

Washington

Docket No. 102994

SAMUEL POORMAN, JR.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Board, as set forth in its Findings of Fact and Opinion promulgated September 12, 1941, it is

Ordered and Decided: That there is a deficiency in income tax for the calendar year 1937 in the amount of \$708.92.

Enter:

Entered Sept. 16, 1941.

(Seal)

ARTHUR J. MELLOTT,
Member. [25]

[Title of Board and Cause.]

PETITION OF SAMUEL POORMAN, JR. FOR
REVIEW, BY THE UNITED STATES
CIRCUIT COURT OF APPEALS FOR THE
NINTH CIRCUIT, OF DECISION OF THE
UNITED STATES BOARD OF TAX AP-
PEALS

Samuel Poorman, Jr., the Petitioner in this cause, appearing herein pro se, hereby files his Petition for a Review, by the United States Circuit Court of Appeals of the Ninth Circuit, of the decision of the United States Board of Tax Appeals entered herein on September 16, 1941, ordering and deciding that there is a deficiency in United States individual income tax due from Petitioner for the calendar (and taxable) year 1937 in the amount of \$708.92; and in that behalf Petitioner respectfully shows:

I.

Petitioner is an individual and a citizen of the United States with residence at No. 1256 West 7th

Street, in The City of Los Angeles, State of California. The United States individual income tax return of Petitioner for the calendar year 1937, in respect of which the aforementioned [26] deficiency has been so determined to have arisen, was duly filed by Petitioner within the time provided therefor with the Collector of Internal Revenue for the Los Angeles Division, 6th District of California, at The City of Los Angeles, State of California, located within the judicial circuit of appeals for the Ninth Circuit.

II.

Nature of the Controversy

The tax in controversy is United States individual income tax for the calendar year 1937 in the principal amount of \$708.92 (less the portion of said amount assessed and/or assessable by reason of the inclusion in Petitioner's taxable income of the sum of \$18.45, for the deduction of which from gross income Petitioner's claim has been abandoned), and such controversy involves the proper determination of Petitioner's liability for such income tax.

Said decision of said Board that there is such deficiency in income tax in the aforesaid amount in controversy is based upon its determination (as set forth in its Findings of Fact and Opinion reported in 45 Board of Tax Appeals Reports, No. 15), that the sum of \$8,394.92, paid to the Petitioner during said year by Los Angeles Gas and Electric Corporation, constituted additional compensation for past

services rendered by Petitioner to said Corporation and was not an absolute gift. [27]

III.

Petitioner, being aggrieved by the said decision of said Board and its said Findings of Fact and Opinion, desires to obtain a review thereof by the United States Circuit Court of Appeals of the Ninth Circuit.

IV.

Assignment of Errors

As the basis of this Petition for Review, Petitioner assigns as error the following acts and omissions of said Board in making its said determination and decision, to wit:

(1) Said Board erred in finding and determining that said sum of \$8,394.92 constituted additional compensation paid to Petitioner by said Los Angeles Gas and Electric Corporation, his former employer, for past services by him rendered to such former employer, and in determining that said sum constituted taxable income of Petitioner for said year 1937;

(2) Said Board erred in failing to find and determine that such payment was a gift to Petitioner and to determine the same to be non-taxable income of Petitioner for said year 1937;

(3) Said Board erred in finding and determining that there was or is a deficiency in said income tax due from Petitioner for said year 1937 by rea-

son of said payment to him of said sum of \$8,394.92; and

(4) Said Board erred in failing to find and determine that there was and is no deficiency in income tax due from [28] Petitioner for said year 1937 by reason of said payment to him of said sum of \$8,394.92.

Wherefore, your Petitioner prays that the Honorable, the United States Circuit Court of Appeals for the Ninth Circuit may review, and reverse and set aside, said decision and order of the United States Board of Tax Appeals insofar as the same relate to said payment to Petitioner of said sum of \$8,394.92 and to any deficiency in income tax due from Petitioner based thereon, and direct said Board to make its decision and order that there is no such deficiency; and that said Court make and enter such further order and direction as may be meet and proper in the premises.

SAMUEL POORMAN, JR.

Petitioner Pro Se

State of California,
County of Los Angeles—ss.

Samuel Poorman, Jr., being first duly sworn, deposes and says: I am the Petitioner in the above-entitled proceeding. I prepared the foregoing Petition and am familiar with the contents thereof, and the allegations of fact contained therein are true to the best of my knowledge, information and belief.

This Petition is not filed for the purpose of [29] delay and I believe that, as such Petitioner, I am justly entitled to the relief sought.

SAMUEL POORMAN, JR.

Subscribed and sworn to before me this 28th day of November, 1941.

(Seal)

E. L. McMURRIN

Notary Public in and for the County of Los Angeles,
State of California.

[Endorsed]: U. S. B. T. A. Filed Dec. 5, 1941.

[30]

[Title of Board and Cause.]

NOTICE OF FILING

To Commissioner of Internal Revenue, Internal Revenue Building, Washington, D. C., and to Chief Counsel of the Bureau of Internal Revenue, Attorney for Respondent, Internal Revenue Building, Washington, D. C.:

You are hereby notified that on the 1st day of December, 1941, a Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of the United States Board of Tax Appeals, heretofore entered in the above-entitled cause, was deposited in the post-office at The City of Los Angeles in a sealed envelope, with the postage thereon fully prepaid, addressed as follows: "United States Board of Tax Appeals, Washington, D. C.", and that with said

Petition was enclosed a request that the same be filed with said Board. A copy of said Petition is attached hereto and served upon you.

Dated at Los Angeles, California, this 1st day of December, 1941.

SAMUEL POORMAN, JR.

Petitioner Pro Se.

[Endorsed]: U. S. B. T. A. Filed Dec. 5, 1941.

[31]

[Title of Board and Cause.]

AFFIDAVIT OF SERVICE BY MAIL

State of California,
County of Los Angeles—ss.

Frantz B. Lilloe, being duly sworn, deposes and says: That he is a citizen of the United States and a resident of The City of Los Angeles, County of Los Angeles, State of California, over the age of 18 years and not a party to the above-entitled proceeding; that on the 1st day of December, 1941, affiant served the within Petition for Review, and also the within Notice of Filing of said Petition, on J. P. Wenchel, Esq., the attorney of record for Respondent therein, by depositing a true copy of each thereof in the postoffice at said City of Los Angeles in a sealed envelope, with the postage thereon fully prepaid, addressed as follows: "J. L. Wenchel, Esq., Chief Counsel, Bureau of Internal

Revenue, Internal Revenue Building, Washington, D. C.", said address being the true address of the party served and the place whereat he has his office. [32]

That the Petitioner in said proceeding resides and has his office in said City of Los Angeles, and that there is a regular communication by mail between such place of mailing and the place to which such envelope was so addressed.

FRANTZ B. LILLOE

Subscribed and sworn to before me this 1st day of December, 1941.

(Seal)

E. L. McMURRIN

Notary Public in and for the County of Los Angeles,
State of California.

[Endorsed]: U. S. B. T. A. Filed Dec. 5, 1941.

[33]

[Title of Board and Cause.]

STATEMENT OF EVIDENCE

The above-entitled cause was heard before the United States Board of Tax Appeals at Los Angeles, California, on February 18, 1941, Hon. Arthur J. Mellott presiding. The following is a statement of the evidence introduced at such hearing.

SAMUEL POORMAN, JR.,

the Petitioner, as a witness in his own behalf, being duly sworn, testified as follows:

Direct Examination

I am the Petitioner, an attorney at law, now Assistant City Attorney of Los Angeles assigned to duty with the Department of Water and Power of the City. For some seventeen years, ending January 31, 1937, I was employed as an attorney in the Legal Department of Los Angeles Gas and Electric Corporation. On that date was consummated a sale to the City of the electric properties of said Corporation, and thereupon some 840 employees of the Corporation were transferred to the City's Department of Water and Power,—myself amongst them, although I did not enter the [34] Department's employ until March 1, 1937.

I had been carrying on the Corporation's franchise litigation against the City for some eight years prior thereto. On January 25, 1937, A. B. Day, then President of the Corporation, called me into his office and told me that my work with it was finished, and that Mr. Robinson, attorney for said Department, who had been my opponent in the franchise cases that had been brought by the City, two in number, had asked if there was anybody to be transferred from the legal department to the Department of Water and Power, that I should be transferred. Mr. Day then said that Pacific Lighting Corporation, which held all of the common stock of Los Angeles Gas and Electric Corporation, had

(Testimony of Samuel Poorman, Jr.)

arranged for the giving of a bonus to the employees transferred to the Department and he advised me what the payment to myself would be. He made no mention of the payment being additional compensation, but he did say that it was in recognition of my fine work in the franchise cases.

On January 30, 1937, I received from Los Angeles Gas and Electric Corporation my last salary check from them, which was at the rate I had enjoyed since 1929, to wit, \$1,000.00 a month. To the check was attached a voucher reading:

“Statement of Account. In full settlement of which Payee has accepted Los Angeles Gas and Electric Corporation check annexed hereto. Samuel Poorman, Jr., January 30, 1937. Services as attorney during month of January, 1937, . . . \$1,000.00. Payee will please detach and retain this statement.” [35]

On February 19, 1937, I received from Los Angeles Gas and Electric Corporation their check payable to me for \$8,394.92, which check I deposited in my account with the Security First National Bank on February 19, 1937. Attached to the check was the following voucher:

“Additional compensation for services to and including January 31, 1937, in accordance with the President’s letter of January 25, 1937. No. 26. Total Amount, \$8,491.34. Deductions, Federal O.A.B. \$20.00. State U. I., \$76.42 Net

(Testimony of Samuel Poorman, Jr.)

Amount, \$8,394.92. This statement constitutes a valuable record of your earnings and the contributions you have made toward future social security benefits. We recommend that you keep it for your future reference. Los Angeles Gas and Electric Corporation. Detach before presenting for payment." (Petitioner's Exhibit 2)

I received Mr. Day's letter (Petitioner's Exhibit 3), referred to in the voucher check, subsequent to my conversation with him. My recollection is that it was after I had left the employ of the Corporation and about the same time that I received a letter dated simply January, 1937, addressed by the Secretary of the Benefit Committee "To members of Uniform Pension and Benefit Plan, who will transfer to the service of The City of Los Angeles concurrently with the transfer of our Electric System to the City," relative to the refund of my contributions to such Plan. (Petitioner's Exhibit 4) Petitioner's Exhibit 3 was the first intimation that I had from any officer of the Company that the payment that had been promised me of \$8,400.00 plus was to be regarded as further compensation, in so many words; but I repeat that when I was told by Mr. Day that Pacific Lighting Corporation had arranged to give a bonus to the departing employees, Mr. Day, said so [36] far as I was con-

(Testimony of Samuel Poorman, Jr.)

cerned, it was in recognition of my fine service in the franchise cases.

Los Angeles Gas and Electric Corporation made a "Severance Report" to the State authorities, a copy of which I received, stating that wages paid me subsequent to January 1, 1936, aggregated \$13,000.00 (Petitioner's Exhibit 5). The Uniform Pension Plan, so far as communicated to the Corporation's employees, was set forth in a pamphlet dated September 1, 1932, of which I received a copy. (Petitioner's Exhibit 6)

In Schedule H, attached to my income tax return for 1937, being the non-taxable income other than interest reported in Schedule B, I reported said payment of \$8,394.92 with the following statement:

"Bonus received from Los Angeles Gas & Electric Corporation after leaving its employ upon transfer of its electric system to the City of Los Angeles, (not having been paid or received as a consideration for service rendered and the same constituting a gift, as held in *Bogardus v. Commissioner of Internal Revenue*, U. S., 82 Lawyers' Edition 90)."

Los Angeles Gas and Electric Corporation was the principal subsidiary of Pacific Lighting Corporation, which owned all of its common capital stock, and the Board of Directors of the subsidiary were the nominees in all instances of Pacific Lighting Corporation. So that is what I would have expected

(Testimony of Samuel Poorman, Jr.)

from Mr. Day when he stated to me that the Pacific Lighting Corporation had arranged to pay a bonus or give a bonus to the departing employees. The common stock held by Pacific Lighting Corporation exceeded the issued preferred stock of Los Angeles Gas and Electric Corporation, the management and control of which was completely dominated by the holding company. At no time did [37] the earnings of Los Angeles Gas and Electric Corporation fail to suffice to cover several times the preferred stock dividend.

I never rendered any service for Los Angeles Gas and Electric Corporation that I was not paid for month by month during the entire period of my employment from June 1, 1920 to January 31, 1937, and since the summer or spring of 1929 my compensation was one thousand dollars a month except for a short time during the worst of the depression when I suffered a 10% reduction. There was never any hold-over of payment or compensation from one month to the next. I was always paid in full for my services of the preceding month, and I had no term of employment with them whatever. It was entirely at their will. I never rendered any services to the Department of Water and Power for the so-called bonus that was paid to me by the Los Angeles Gas and Electric Corporation, nor did I promise to enter the employ of that department. There was no strings whatever attached to the payment of the \$8,400.00 plus, and no services that I

(Testimony of Samuel Poorman, Jr.)

rendered after its payment, no services that I rendered especially in the week after I was advised that my employment would end with the month of January 1937. I went about my ordinary affairs which at that time was principally taking care of odds and ends and trying to get them as far in shape as one could before he left an office with which he has been long associated.

The Corporation's employees transferred to the Department of Water and Power on the sale of the former's electric plant constituted about a third of the personnel. None of the two-thirds that remained with the corporation received any such bonus. [38]

Thereupon, Petitioner's Exhibits, 1, 2, 3, 4, 5 and 6, heretofore mentioned, were received in evidence.

Petitioner's Exhibit 3 is as follows:

Los Angeles Gas and Electric Corporation

January 25, 1937

Office of

President and General Manager

To Employees about to be transferred from the
Service of our Company:

You are all familiar with the recent events which have resulted in the sale of our electric properties to the City of Los Angeles, and which will make it necessary that the people who operate these properties sever their rela-

(Testimony of Samuel Poorman, Jr.)

tions with Los Angeles Gas and Electric Corporation.

At this time and just before the transfer is completed, I want to express to you all my very great appreciation of the splendid service you have rendered during the past many years, and of the fine support you have given to me and to our management generally in the conduct of our electric business. I have been very happy indeed because of the good-fellowship and spirit of friendliness which has always existed between us, and regret more than I can tell you the conditions which make it impossible for us to continue working together.

Arrangements have been made to grant you additional compensation in recognition of the value of your past services. The amount of this payment will be based upon your present attained age, your length of service with the Company, and the rates of wages received during your period of employment; but this extra compensation will not be paid to employees whose "employment date" is more recent than September 1, 1934. Checks will be mailed to you as soon as possible after our electric properties have passed to the City.

I believe that those of you who enter the employ of the Bureau of Power and Light will be happy in your new environment, and will do well in that field of endeavor. You have my

(Testimony of Samuel Poorman, Jr.)

every wish for your future and continued success.

Sincerely,

(Signed) ADDISON B. DAY

President and General Manager [39]

Petitioner's Exhibit 4 is as follows:

Los Angeles Gas and Electric Corporation

January 1937

Office of

Personnel Manager

To Members of Uniform Pension and Benefit Plan Who Will Transfer to the Service of the City of Los Angeles concurrently with the Transfer of Our Electric System to the City:

As you undoubtedly are aware, your membership in Uniform Pension and Benefit Plan will cease with the termination of your service with Los Angeles Gas and Electric Corporation. Your life insurance protection under the Plan will continue for 31 days after termination of service.

As soon as possible after the transfer, a check will be sent you covering the item of the refund of your contributions to the Plan, now in the hands of Metropolitan Life Insurance Company, together with interest thereon.

Your attention is called to the section entitled "Employee Options upon Termination,"

(Testimony of Samuel Poorman, Jr.)

to be found on pages 14 and 15 of the "Announcement of Uniform Pension and Benefit Plan." Briefly, you have the right to leave your contributions with Metropolitan Life Insurance Company, instead of withdrawing them, and instead—

(a) receive a monthly income for life (pension), to begin at your normal retirement date, or,

(b) continue your contributions to the Insurance Company direct, to purchase a retirement income or pension, to begin at your normal retirement date.

Also, you can arrange with the Insurance Company to change your life insurance, without medical examination, into some form of life insurance policy issued by that Company.

In case you desire to take advantage of any of these options, you should make your intentions known to the office of the Secretary, Mr. F. E. Seaver, who will give you more detailed instructions as to procedure. In any event, please locate your Pension and Benefit Plan Certificate, immediately, and have it ready to turn in when called for. [40]

Any questions regarding the foregoing matters will be answered cheerfully.

Sincerely,

(Signed) D. L. SCOTT

Secretary Benefit Committee

(Testimony of Samuel Poorman, Jr.)

Petitioner's Exhibit 5, severance report made by Los Angeles Gas and Electric Corporation to State authorities in respect to Samuel Poorman, Jr., Attorney. Under heading: "Submit data subsequent to January 1, 1936", the following is shown: date of severance January 30, 1937; total hours worked 2152; total weeks worked 57; wages paid \$13,000; other remuneration \$8,491.34; total wages paid \$21,491.34; amount of contributions deducted \$139.42.

The following excerpts are taken from pages 14 to 17, inclusive, of Petitioner's Exhibits 6:

"Employee Options Upon Termination

Certificate from Insurance Company—

The Insurance Company will issue to each employee participating in the plan a certificate guaranteeing the return, in the manner herein provided, of the entire amount contributed by the employee with interest at the rate of 3% on contributions which have been in the hands of the Insurance Company for a full 12 months' period, compounded at the end of each completed year of participation in the plan.

Options Upon Withdrawal from Service—

If, prior to normal retirement date, an employee withdraws or is released from service, or does not return to service upon discontinuance of disability payments, his total contributions with interest will be returned to him in cash, but such employee shall have the option to

(Testimony of Samuel Poorman, Jr.)

leave such contributions with the Insurance Company and receive therefrom a monthly income [41] for life from normal retirement date, to the extent provided by such contributions, with interest, or to continue his contributions to the Insurance Company and receive therefrom a monthly income for life from normal retirement date, to the extent provided by such contributions with interest.

Privilege of Converting Death Benefits Upon Withdrawal from Service—

If, prior to normal retirement date, an employee withdraws or is released from service, such employee may at his option convert his death benefit into any of the regular life insurance policies issued by the Insurance Company, term insurance excepted, at the rate applicable to his then attained age and class of risk. Such conversion may be effected without medical examination provided application is made within 31 days after termination of service.

Death—Prior to Retirement—

Upon the death of an employee prior to normal retirement date, his total contributions with interest will be returned to beneficiaries in cash.

Death—After Retirement—

Upon the death of an employee subsequent to normal retirement date, the difference, if

(Testimony of Samuel Poorman, Jr.)

any, between the employee's total contributions, with interest to normal retirement date, and the total pension or disability retirement income the employee has received up to date of death will be returned to beneficiaries in cash.

“General Provisions

In the Event of Change or Discontinuance—

As the result of careful study and preparation, this Company has been able to prepare a plan which it desires and expects to continue indefinitely into the future. * * * Nevertheless, the Company must and does reserve the right to discontinue or change the plan at any time. Discontinuance or change, however, will neither deprive any employee of any right with respect to his contributions nor affect retirement annuities which have been purchased prior to the date of discontinuance or change. The Company's contributions, once made, will be used for employees' benefits and for no other purpose.

Not an Employment Contract—

Neither the action of the Company in adopting this plan nor any action taken by the Benefit Committee in interpreting its provisions or in granting benefits hereunder, shall be construed as giving to any officer, agent or employee of the Company the right to be re-

(Testimony of Samuel Poorman, Jr.)

tained in the service, nor shall any [42] employee, after termination of service, have any rights whatsoever hereunder, enforceable either at law or in equity, except as hereinabove expressly provided under the heading 'Employee Options upon Termination.' "

W. E. HOUGHTON,

called by Respondent as a witness, having been duly sworn, testified as follows:

Direct Examination

I am one of the Vice Presidents of Southern California Gas Company, the successor by merger in May, 1937, to Los Angeles Gas and Electric Corporation. On January 31, 1937, and for a number of years prior thereto, I was a Vice President and Treasurer of the latter corporation, and also Chairman of the Committee administering its Pension and Benefit Plan. The Los Angeles Gas and Electric Corporation transferred its electrical properties to the City of Los Angeles and retained its gas properties. The negotiations which ultimately led to the sale of the electric properties were carried on for at least a year and a half, the final agreement being completed and executed in October, 1936. Mr. Poorman had much to do with that matter, as well as other attorneys. The question whether or not cer-

(Testimony of W. E. Houghton.)

tain employees would be transferred to or taken over by the City did come up quite early in the negotiations, because the condition of the City taking over the employees with the property, was one of the essential factors in the whole deal. In fact the Los Angeles Gas and Electric Company's officers were quite insistent from almost the start that they wouldn't talk seriously of a deal with the City unless the City would take the employees to operate the property taken over, because it would be very difficult for the remaining Gas Department to absorb them and the Company [43] certainly did not want to see them left without occupations. The employees taken over were connected primarily with the Electric Department of the old company, but with certain classes of employees a more or less arbitrary allocation had to be made.

Consideration was given to the possible effect of the transfer of employees upon their so-called pension rights, quite early in the course of the proceedings, because it was recognized that in accordance with the terms of the Pension Plan, severance of employment meant sacrifice of not only pension rights, but all rights under the pension benefit plan, with the exception that the life insurance was continued for 31 days after such severance. It was recognized that the employees were losing various rights in leaving the service of the Corporation. About the middle of 1936, when it looked quite cer-

(Testimony of W. E. Houghton.)

tain that the deal for the sale of the property to the City would ultimately be consummated, consideration commenced among the company officials as to what, if anything, could be done for the employees who were transferred to the City with the property or at the same time as the property, in consideration of the fact that they were going to lose their pension rights by termination of service. Various discussions were held among company officials, principally Mr. Day, the President, Mr. Masser, the Executive Vice President, Mr. Hornby, one of the Vice Presidents of Pacific Lighting Corporation, the Parent Company, and myself, and, in some of the discussions, one or two others. I have in mind particularly Mr. Scott, the personnel manager of the Corporation. The first discussion centered more or less around the possibility of obtaining from the Metropolitan Life Insurance Company, which underwrote [44] the Pension Benefit Plan, some sort of a continuing benefit under the Plan. The plan would have to be seriously amended and it didn't when mentioned to the representatives of the insurance Company meet at all with their favor. In fact they said it was impossible, that we had just better do directly for the departing employees whatever the company could and desired to do. After much discussion, the plan ultimately followed was worked out and a basis of additional compensation for past services was formulated which, as stated in the

(Testimony of W. E. Houghton.)

President's letter, was in consideration of past valuable services and was based upon the present attained age of the employees, their length of service with the company, and the rates of wages which they had received during their period of employment. I think I made the original draft of the proposed letter for Mr. Day to send out and that was revised a number of times and finally resulted in the letter in the form as sent out under date of January 25, 1937 (Petitioner's Exhibit 3).

In a general way I had something to do with the letter identified as Petitioner's Exhibit 4; largely for the reason that the carrying out of the mechanics of this matter of issuing the additional compensation checks was under my supervision, and I knew that this certain letter, the one signed by Mr. Scott, was being prepared. In fact, I think I had a hand in preparing it. And to the best of my recollection, the two letters (Exhibits 3 and 4) were sent out in the same envelope, although I couldn't definitely say that that was the case. I might put it this way: We had a regular mailing list of the employees, and a set of envelopes for sending out such letters as this were always prepared well in advance of the actual date of mailing in order that there be no delay when a thing of this kind is ready to go. [45] The company was particularly anxious—and I know of this of my own knowledge—to have this information, the substance of this letter, reach the employees certainly before they completed their

(Testimony of W. E. Houghton.)

service with the company, because, oh, I should say at least three or four weeks before this letter was sent out we commenced to get inquiries from our employees as to "when is the bonus going to be paid? When is the additional compensation going to be paid?" A thing of that kind soon gets around that something is going to be done. So the company was most anxious that the word get to them definitely as early as was possible; and for that reason, although I can't say that the letter was mailed on Janaury 25th, it is very probable that it was mailed on that date. It was certainly the corporation's intention to have the employees notified before they left its own service. And that is the main reason why I think this letter was mailed either on January 25th or the next day.

Thereupon, there was received in evidence Respondent's Exhibit A, being cancelled check of the Los Angeles Gas and Electric Corporation, dated February 17, 1937, and payable to the order of Samuel Poorman, Jr. \$8,394.92, additional compensation for services to and including January 31, 1937. To this check was attached voucher identified as Petitioner's Exhibit 2.

Thereupon Petitioner admitted that the language on the prior checks was always of the type of language in Petitioner's Exhibit 1: "Services as attorney during the month of January," or whatever date it was, at the rate.

(Testimony of W. E. Houghton.)

Most careful consideration was given to both the language used on the check (Exhibit A) in describing this payment, [46] as well as the language used in the letter sent out by the president (Exhibit 3). The desire was to make the language used as accurately descriptive as possible, and it was felt that the language used did fall in that category inasmuch as the extra compensation was based on the length of past service, that is, service prior to January 31, 1937, upon the rate of the pay received by the employee during all that period, and the desire was that there be no question in the minds of anyone examining the books and records that the payments were additional compensation rather than of any other nature. That phraseology or similar phraseology runs through all of the record with references to these payments.

The main purpose in sending the second letters (Exhibit 4) was to avoid any possible misunderstanding on the part of the employees as to just exactly what the payments were that they were going to receive. There was one other little reason that entered into the matter, as I recall. While almost all of the employees of the corporation who were transferred to the City were entitled to this bonus or additional compensation, there were a few who were not entitled to it, but who had been contributors to the Pension and Benefit Plan and who received a refund of their contributions to the Plan.

(Testimony of W. E. Houghton.)

But the main purpose was, as I stated first, to avoid any misunderstanding, to have one letter definitely state that they were receiving back, or going to receive back, their own contributions to the pension benefit plan, together with interest, as provided in that plan; and the other letter to show what they were going to, or at least the basis on which they were going to receive additional compensation for.

[47]

Not to my recollection was Mr. Poorman called into any of these discussions that I mentioned at which time some three or four of the company officials were present. It may be quite possible that Mr. Day or Mr. Masser, the Executive Vice President whom I mentioned, may have discussed the matter with him. I have no information as to that.

For 1937 as well as for many years past, the preparation of the old Company's federal income tax returns was directly under my supervision, and I actually did a lot of detailed work. I may have on occasion, and I think I did in some prior years, go to Mr. Poorman for his opinion or advice with respect to certain tax matters involved in the particular year's return. I don't recall that I consulted him with respect to the 1937 return, and I am quite sure that I didn't for this reason: Along about, oh, I should say 1935, Pacific Lighting employed a firm of tax attorneys for the purpose of furnishing advice to itself and to its subsidiary companies

(Testimony of W. E. Houghton.)

with respect to the filing of their income tax returns, and also the handling of any developments subsequent to the filing of the returns leading up to the settlement of the tax cases, so that from somewhere around 1935—it may have been a little earlier—tax matters generally were referred to this outside firm of tax attorneys.

I have with me the record of the Corporation that relates to this disbursement to Mr. Poorman. The Corporation's original record consisted of a list by names of the individual employees to whom these additional compensation payments were made, showing in each case the total amount of their regular wages during their past service. In the next column, the amount of the extra compensation to be paid them, followed by certain deductions for [48] Federal old age benefits and state unemployment insurance tax, arriving in the right-hand column at the net amount paid them as shown by the individual checks. Over across the back of this list appears the name of Samuel Poorman, Jr., showing the gross amount of his check, as is already in the record, together with the two deductions mentioned, arriving at the net amount of \$8,394.92. This is the preliminary record, and the total of the payments to the 800 odd employees is shown here as \$475,546.32. That amount divided into two items, as I will show, was charged to a ledger account designated as "Sale of Electric Properties, suspense account." This account showed

(Testimony of W. E. Houghton.)

in black entries the total expenses in connection with the sale of these properties. It showed in red ink figures the amount received from the City for the properties, together with any other credits necessary in order to arrive at the net profit, net credit resulting from this sale. This total amount of extra compensation, additional compensation, is represented by two vouchers covering the deposit of the amount of money in a special bank account against which these individual employee checks were drawn. The first voucher is dated February 17, 1937, in the amount of \$473,702.47, and duly entered as a debit or expense item in black ink in this special ledger account. The balance making up the grand total previously mentioned, this balance being \$1,843.85, is covered by a voucher dated February 27, 1937, and duly entered in a similar manner in this same ledger account. The record shows that at the close of February the net balance was transferred to surplus account in the amount of round figures, \$6,100,000, resulting from the sale of those electric properties at an agreed price of \$46,000,000 plus. That net balance was the profit [49] figured on the sale up to that time based on the expense items that had come through and been paid and after providing an estimated reserve for federal income taxes and state bank and corporation franchise tax upon the profits. That was the estimated net profit transferred to surplus. However, following on during March and April were some additional strag-

(Testimony of W. E. Houghton.)

gling amounts of expense which we hadn't been able to ascertain accurately at an earlier date that were charged to this account and also a clean-up sale of materials and supplies to the City of Los Angeles, supplies applicable to the electric properties, that resulted in an additional surplus credit of \$20,813. So that these additional compensation expenditures in question were definitely charged to expense; although it is not particularly relevant here, in the consideration later of its own income tax return these extra compensation payments were allowed as proper expenses in arriving at taxable net income. This language that is quoted of additional compensation, as I said, runs through all the records. On these two vouchers on which I have just testified, the same language appears, "Additional compensation for past services" and so forth. The company made out its federal income tax return in accordance with this same treatment of this particular item. There were certain charges made to this account which were not proper deductions for Federal income tax purposes, but so far as this item of additional compensation is concerned, it is treated exactly as it runs through all of the records. [50]

Cross Examination of W. E. Houghton

The Corporation's return for 1937 shows net income for excess-profits computation to be \$15,487.429.60, and Schedule E attached to the return shows a taxable profit from the sale of electric properties of \$13,360,895.75, which is part of said fifteen mil-

(Testimony of W. E. Houghton.)

lion dollar item. Said Schedule E shows the expenses of sale, \$3,306,000.00, and the items back of that include this extra compensation. This deduction comes as a deduction as against the sale of capital assets and not as a deduction in respect of ordinary operating expenses. We intentionally set out on our books our regular operations separate and apart from the profit resulting from the sale of the Electric properties, and in our return in Schedule E we set out the same thing, the sale of the electric properties entirely separate from regular operation. In respect of ordinary operations to the best of my knowledge, no extra compensation was ever accorded the Petitioner at any time during his employment by Los Angeles Gas and Electric Corporation, otherwise than by antedating for three months an increase in salary granted to him in 1929. I don't recall any payments that the Petitioner ever received from the company other than his monthly salary prior to the payment here in question.

Q. (By Mr. Poorman) Now, how is it that no part of this additional compensation was reflected in the ordinary operating expenses of the Corporation covering any period of time if, indeed, it was extra compensation for services rendered by the Petitioner.

A. Well, in the first place, the company's books for all years past in 1937 had been definitely closed at the time that the determination

(Testimony of W. E. Houghton.)

was definitely made to pay this amount of extra [51] compensation, so that it would have been impossible to go back even had they so desired and pro-rate or apportion this to any prior period of years.

Q. Well, then, for the tax year 1937, why was that not made as a charge in the nature of ordinary operating expenses?

A. Well, it was so definitely not ordinary operating expenses; it would never have been made except for the sale of the electric properties or some other abnormal or extraordinary transaction.

To my knowledge Petitioner had little or nothing to do with the sale of electric properties. So far as I know he did not. But this item, as I have testified, was charged against the expenses of sale and was one of the items deductible from the gross proceeds of that sale in order to determine the profit on the sale. Everything considered, I think it was a pretty good sale. The Corporation had been subjected to long drawn out and expensive litigation in which its rights to use the streets to distribute either gas or electricity for other than lighting purposes had been brought in question. The Petitioner was almost exclusively engaged in work in that litigation from 1927 until the sale was effected, and that is why I stated I did not think he had anything to do with the negotiations for the sale of the electric properties.

(Testimony of W. E. Houghton.)

The determination to make the payments to the transferred employees in the form of additional compensation was arrived at some time in late November, 1936, or early December. The agreement of sale was executed along about October 22, 1936, but before that sale could be effected there had to be an election and a voting upon the bonds necessary to effect the purchase by the City, which was held in the middle of December, 1937 (1936). So that [52] until that election occurred no one knew definitely that there would be a sale under the then pending negotiations.

So far as I know, Petitioner had nothing whatever to do with any of the conferences respecting pension matters, or the taking over of employees by the City. In these conferences with respect to deciding on some sort of a payment to the employees, Petitioner did not participate.

Q. (By Mr. Poorman) And what was it that led to the adoption of the characterization of this payment as additional compensation other than the fact that you could not make suitable arrangements for the carrying on of some sort of pension arrangement by the Metropolitan Life Insurance Company in favor of the transferred employees?

A. Well, since we have mentioned the tax angle, that came into the consideration to make the payment in such manner as would be considered a proper deductible expense.

(Testimony of W. E. Houghton.)

Q. Of the Corporation?

A. Of the Corporation.

Q. As against the profit on the sale.

A. That is true.

There would be no question of the so-called compensation except for the sale of the electric plant to the City. There was no question of the extra compensation of the employees retained by the Corporation.

Q. Is there any account with respect to the account that you have already testified, that is, the account having to do with the profit on the sale of the electric plant, in which any portion of the so-called extra compensation paid to the affected employees is reflected?

A. No other account.

To the best of my recollection I had not consulted with the Petitioner on any point in connection with the Corporation's 1937 income tax return. The Petitioner had no connection with the [53] merger of Los Angeles Gas and Electric Corporation with Southern California Gas Company in May, 1937. The preparations for that merger didn't commence until after the conclusion of the sale of the electric properties to the City on the last day of January, 1937.

(Testimony of W. E. Houghton.)

Redirect Examination of W. E. Houghton

Mr. Poorman, at the time of this sale of assets in January, 1937, was one of the regular salaried attorneys working under the General Counsel of the Company in the Legal Department. The General Counsel was located in the same office building and the same department in which Mr. Poorman worked. The last four or five years, three or four years, of Mr. Poorman's connection with the Corporation were spent exclusively or practically exclusively in connection with the franchise litigation against the Company by The City of Los Angeles with reference to both its gas and electric franchises. To the best of my knowledge, in that connection Mr. Poorman had decidedly rendered satisfactory services. And all during his service for the Company, he certainly had been a valuable employee. As to Mr. Poorman's increase in salary in 1929, I don't think there is any question on anybody's part but that it was regular salary and made retroactive for the entire calendar year.

SAMUEL POORMAN, JR.,

the Petitioner, re-presenting himself as a witness in his own behalf, testified further as follows:

Direct Examination

From August, 1927, forward until the conclusion of the Pasadena franchise case, I was engaged almost exclusively on the Los Angeles Electric franchise case, the Los Angeles gas franchise [54] case, and the Pasadena gas franchise case, the last of which was decided about December, 1935. I had already appealed in the Los Angeles cases and, after perfecting the record on appeal, was engaged in writing the brief, which was a voluminous matter and occupied me right up to the time I left the Corporation. I had none of its general affairs in my hands, although any officer might ask me some detached question from time to time, but nothing that required research or any extensive draftsmanship did I do for the Company after I became interested in the electric franchise case, except for a period of about six months following the bursting of the St. Francis Dam in 1927, when the City had so many troubles on its hands that the then pending franchise case became quiescent. That was the only time I had taken up general work after the franchise cases started, except for the sporadic questions that came up. I participated in none of the negotiations that resulted in the sale of the electric properties to the City.

The parties agree that the foregoing is all of the evidence adduced at the hearing before the United States Board of Tax Appeals material to this proceeding.

SAMUEL POORMAN, JR.,

Petitioner on Review.

J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

[Endorsed]: U.S.B.T.A. Filed March 3, 1942. [55]

[Title of Board and Cause.]

PRAECIPE FOR RECORD.

To the Clerk of the United States Board of Tax Appeals, Washington, D. C.:—

You are hereby requested to prepare and certify, and to transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, in the manner and within the time required by law and the rules of said Court, a typewritten copy of the Record on Review under Petitioner's Petition for Review of the Decision of the United States Board of Tax Appeals in the above-entitled cause, and to include therein a copy of each of the following entries and documents, to-wit:

1. The docket entries of all proceedings before the Board of Tax Appeals.
2. The pleadings before said Board, as follows:

(a) The Petition for Redetermination of
Deficiency;

(b) The Answer of Respondent thereto.

[56]

3. The Findings of Fact and Opinion of said
Board.

4. The Decision of said Board.

5. The Petition for Review of said Decision.

6. The Statement of Evidence on review, as
approved.

7. This Praeipice.

SAMUEL POORMAN, JR.,

Petitioner pro se.

Address: 1256 West 7th Street, Los Angeles, Cali-
fornia.

[Endorsed]: U.S.B.T.A. Filed Jan. 10, 1942. [57]

[Title of Board and Cause.]

CERTIFICATE.

I, B. D. Gamble, clerk of the U. S. Board of Tax
Appeals, do hereby certify that the foregoing pages,
1 to 57, inclusive, contain and are a true copy of the
transcript of record, papers, and proceedings on file
and of record in my office as called for by the
Praeipice in the appeal (or appeals) as above num-
bered and entitled.

In testimony whereof, I hereunto set my hand and
affix the seal of the United States Board of Tax

Appeals, at Washington, in the District of Columbia, this 4th day of March, 1942.

(Seal)

B. D. GAMBLE,

Clerk,

United States Board of Tax
Appeals.

[Endorsed]: No. 10090. United States Circuit Court of Appeals for the Ninth Circuit. Samuel Poorman, Jr., Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed March 18, 1942.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.